

SERVICE DATE – LATE RELEASE APRIL 13, 2006

SURFACE TRANSPORTATION BOARD

DECISION

STB Docket No. AB-1081X

SAN PEDRO RAILROAD OPERATING COMPANY, LLC—ABANDONMENT
EXEMPTION—IN COCHISE COUNTY, AZ

IN THE MATTER OF A REQUEST TO SET TERMS AND CONDITIONS

Decided: April 10, 2006

By decision served February 3, 2006, the Board, under 49 U.S.C. 10502, exempted from the prior approval requirements of 49 U.S.C. 10903 the abandonment by San Pedro Railroad Operating Company, LLC (SPROC) of approximately 76.2 miles of railroad line in Cochise County, AZ, as follows: (1) the Bisbee Branch, between milepost 1085.0 at Bisbee Junction and milepost 1090.6 at Bisbee, a distance of 5.6 miles; and (2) the Douglas Branch (a) between milepost 1097.3 near Paul Spur and milepost 1106.5 near Douglas, a distance of 9.2 miles, (b) between milepost 1055.8 near Charleston and milepost 1097.3 near Paul Spur, a distance of 41.5 miles, and (c) between milepost 1040.15 near Curtiss and milepost 1055.8 near Charleston, a distance of 19.9 miles. The exemption was subject to public use, environmental, and standard employee protective conditions and was scheduled to become effective on March 5, 2006, unless an offer of financial assistance (OFA) was filed on or before February 13, 2006.

On February 13, 2006, Sonora-Arizona International LLC (Sonora) timely filed an OFA under 49 U.S.C. 10904 and 49 CFR 1152.27(c) to purchase the entire line for \$5,400,000. In a decision served on February 17, 2006, the Board, by the Director of the Office of Proceedings, (1) found Sonora to be financially responsible, (2) denied a SPROC motion to reject the OFA, (3) postponed the effective date of the exemption to permit the OFA process to proceed, and (4) set March 15, 2006 as the due date for any request to establish the terms and conditions for purchase of the line.¹ On March 15, 2006, Sonora filed a petition asking the Board to: (1) clarify the scope of the abandonment and of the property that is the subject of the OFA, and (2) extend the period within which the parties could reach agreement on the terms and conditions for purchase of the line. By letter filed March 16, 2006, SPROC sought rejection of the petition.

¹ Also on February 17, 2006, Union Pacific Railroad Company (UP), a potential carrier on the line according to Sonora, filed a letter stating that it takes no position on the OFA or the abandonment.

By decision served on March 16, 2006, the Board denied Sonora's petition, and extended the due date for a request to set terms and conditions to March 17, 2006.

On March 17, 2006, Sonora filed a motion for leave to file a request to set terms and conditions, as well as a request that the Board set the terms and conditions for the sale of this line. In its request, Sonora reiterates its offer to purchase the 76.2 miles of track and right-of-way (ROW) for \$5,400,000, which it contends was the Net Liquidation Value (NLV) submitted by SPROC in this proceeding in Exhibit F to its petition.² Sonora argues that SPROC is improperly attempting to increase the NLV figure above what it presented to the Board (to \$5,650,000) and to remove two of the line segments from the OFA procedures, reducing the amount of track and right-of-way by 15.3 miles. Sonora also argues that SPROC should not be permitted to limit its exposure for pre-existing environmental conditions to one year following closing and a maximum of \$50,000 of liability. Sonora asks that the Board require SPROC to sell it all four involved line segments at the NLV claimed in the petition for exemption, and to require SPROC to accept Sonora's other terms and conditions.

On March 22, 2006, SPROC replied to the request to set terms and conditions. SPROC contends that the NLV of the line was and is \$5,650,000, consisting of \$5,385,208 (rounded by the appraiser to \$5,400,000) for track and track materials and \$247,436 (rounded by SPROC to \$250,000) for land, based on 1,265 acres of land in the ROW at \$275 per acre. In support, SPROC submits a verified statement from Mr. Kenneth D. Young, who performs rail valuation services and who prepared an appraisal for the track assets of SPROC, and a letter from Mr. Craig Abbott, a real estate broker who prepared an estimate of the fair market value of the right-of-way. Thus, SPROC argues, \$5,650,000 is the price Sonora should be required to pay for this line.

Additionally, SPROC maintains that previous owners of the line abandoned and salvaged the Bisbee Branch and the portion of the Douglas Branch between Paul Spur and Douglas. As a result, SPROC argues that the track from those two segments should be deducted from this sale, reducing the total track mileage from 76.2 miles to 61.4 miles. SPROC adds that a 20-mile portion of the line south of Curtiss is held by easement over property owned by UP. SPROC Petition, Exhibit B at 5. SPROC states, however, that it agrees to sell all operating property it has the legal power to sell and, to the extent it has the power to convey the ROW on the first two segments by quitclaim deed, it will do so. SPROC Reply to Set Terms Request at 6.

SPROC states that Sonora's request that SPROC indemnify it against pre-existing environmental conditions without any apparent limit is contrary to Board policy and contravenes standard railroad industry practice that rights-of-way are sold "as is." Stating that it is concerned about Sonora's ability to close this transaction, SPROC requests that the Board: (1) set an early

² Sonora offers no additional evidence to support its offer; instead, it relies on SPROC's NLV evidence.

closing date, no more than 45 days from the date that Sonora accepts the terms set by the Board; (2) require Sonora to tender to SPROC a nonrefundable deposit of \$150,000 should it fail to close for any reason (other than one caused by SPROC's actions); and (3) require Sonora to deposit the balance of the \$5,650,000 purchase price into an escrow account.

On March 22, 2006, the United States Department of the Interior, Bureau of Land Management (BLM) submitted a comment. BLM states that it "constitutes the majority landowner" of the property adjacent to this line. BLM states that it has long desired to acquire or rail bank the railroad corridor and that it strongly supports the abandonment of the line, the Trust for Public Land's request for a public use condition, and the creation of a trail. BLM also expresses concern about potential future use of the line to transport hazardous materials and, for that reason, supports the immediate denial of Sonora's OFA or, at least, prior detailed environmental review of the proposal. On March 31, 2006 and April 11, 2006, the Center for Biological Diversity (CBD), which describes itself as a group of "... 22,500 members, many of whom recreate and enjoy the San Pedro River and National Conservation Area," filed letters asking us to prepare an environmental impact statement on the effect of Sonora's acquisition of the line. On April 6, 2006, Sonora filed a letter opposing the environmental review sought by BLM and CBD. SPROC filed a letter in response to Sonora's comments on April 11, 2006.

TERMS AND CONDITIONS

Valuation and Evidentiary Standards.

Proceedings to set OFA conditions and compensation are governed by the provisions of 49 U.S.C. 10904(d)-(f). Under section 10904(f)(1)(B), the Board may not set a price that is below the fair market value of the line. In the absence of a higher going-concern value for continued rail use,³ the proper valuation standard in proceedings for offers to purchase under section 10904 is the NLV of the rail properties for their highest and best nonrail use. Chicago and North Western Transp. Co.—Abandonment, 363 I.C.C. 956, 958 (1981) (Lake Geneva Line), aff'd sub nom. Chicago and North Western Transp. Co. v. U.S., 678 F.2d 665 (7th Cir. 1982). NLV includes the value of the underlying real estate plus the net salvage value (NSV) of track and track materials.

The burden of proof is on the offeror, as the proponent of the requested relief. See Lake Geneva Line, 363 I.C.C. at 961. Placing the burden of proof on the offeror is particularly appropriate in forced sale proceedings under 49 U.S.C. 10904 because the offeror may withdraw its offer at any time prior to its acceptance of the terms and conditions that the Board establishes pursuant to a party's request. The rail carrier, on the other hand, is required to sell its line to the

³ The parties do not argue that the line has a going-concern value here. Although an OFA contemplates future rail service, in the absence of a higher going-concern value, we value the line as if it were to be dismantled and taken out of service.

offeror at the price the Board sets, even if the railroad views the price as too low. To determine the NLV, we will address below the parties' evidence on the value of the land and the track and track materials.

Land.

SPROC argues that the Bisbee Branch and the segment of the Douglas Branch between Paul Spur and Douglas should not be included as part of this sale because they were previously abandoned and salvaged. However, the record shows that, although the previous owner of the line, SWKR Operating Co., Inc. (SWKR) obtained exemptions allowing it to abandon the Bisbee Branch and Paul Spur-Douglas segment,⁴ SWKR did not exercise that authority and consummate the abandonments. Rather, the two segments were subsequently rail banked. SPROC Petition, Exhibit B at 2. Thus, the Bisbee Branch and the Paul Spur-Douglas segment were never abandoned by SWKR.

When SPROC obtained authority to acquire and operate this line in 2003, it specifically acquired all of SWKR's interest in the line, as well as common carrier authority to operate over the Bisbee Branch and the entire Douglas Branch. San Pedro Railroad Operating Company, LLC—Acquisition and Operation Exemption—SWKR Operating Co., Inc., STB Finance Docket No. 34430 (STB served Nov. 21, 2003). Therefore, even if SWKR had exercised its abandonment authority, the common carrier obligation to operate over the Bisbee Branch and Douglas Branch would have been reinstituted with SPROC's acquisition and operation exemption.

The fact that some tracks were taken up and portions of the line were salvaged is immaterial. Merely removing track materials does not constitute an abandonment. The Phillips Company—Petition for Declaratory Order, Finance Docket No. 32518 (ICC served Apr. 18, 1995), reopening denied (Feb. 14, 1997). Because both the Bisbee Branch and the Paul Spur-Douglas segment have been operated as part of a regulated, common carrier line of railroad, see SPROC Petition, Exhibit A (map), it may not be abandoned without authority from the Board; see The Atchison, Topeka and Santa Fe Railway Company—Abandonment Exemption—In Lyon County, KS, Docket No. AB-52 (Sub-No. 71X), slip op. at 10 (ICC served June 17, 1991). Thus, removal of the track, by itself, has no effect on the regulatory status of the line. Finally, when SPROC sought abandonment authority from the Board on June 6, 2005, and again on October 17, 2005, its petition included both the Bisbee Branch and the Paul Spur-Douglas segment. SPROC cannot now argue that these segments are not included in this OFA proceeding.

⁴ SWKR Operating Co., Inc.—Abandonment Exemption—In Cochise County, AZ, Docket No. AB-441 (Sub-No. 1X) (ICC served Oct. 12, 1995).

Sonora presents no specific evidence regarding the value of the land, relying instead on the NLV of \$5,400,000 in Mr. Young's appraisal. However, Mr. Young specifically states that his NLV appraisal report "includes only rail, other track material (OTM), switches and ties," and "excludes the underlying land, buildings, rolling stock or maintenance-of-way equipment." SPROC's Petition, Exhibit F, Verified Statement at 2 (emphasis in original). Although Mr. Young's appraisal might, for the Board's purposes here, be more accurately described as a report on the NSV rather than the NLV, a review of the record makes it clear that his appraisal does not include the underlying land. It is therefore appropriate that we consider the value of the land separately.

SPROC has based its valuation of the real estate underlying the line on an estimate prepared by Craig Abbott. Mr. Abbott offers his opinion that the estimated fair market value of the property, as of September 21, 2005, is \$275 per acre. SPROC Petition, Exhibit D, Attachment 18. Based on Mr. Abbott's conclusions, SPROC management values the ROW at \$247,436 (which it rounds to \$250,000) based upon 1,265 acres of land held in fee. However, Mr. Abbott states in his letter that he did not make a personal inspection of all of the subject property covered in his report and did not conduct a land survey or title search.

For purposes of computing NLV, we assign value only to land to which a railroad holds marketable title. Marketable title generally means that held by warranty or quitclaim deed without restrictions or reversionary language. Thus, property that is subject to a reversion, if no longer used for rail purposes, or if held by easement for railroad purposes, is not included in determining real estate NLV. Southern Pacific Transportation Company—Abandonment Exemption—Sacramento and El Dorado Counties, CA, Docket No. AB-12 (Sub-No. 159X) (ICC served Oct. 20, 1994) (Southern Pacific). Although Mr. Abbott's valuation of the land at \$247,436,⁵ is uncontested, SPROC has presented no evidence of marketability of title to the 1,265 acres it claims to hold in fee. We will therefore accept Mr. Abbott's figure, on the condition that SPROC indemnify Sonora in full for any defect in title. If SPROC declines to provide such an indemnity for the 1,265 acres of land held in fee, the title to that land will be deemed not marketable and will be assigned no value. See Union Pacific Railroad Company—Abandonment—In Polk County, IA, STB Docket No. AB-33 (Sub-No. 170) (STB served June 19, 2002) (citing Southern Pacific). Warranty of title, for example, would be acceptable as indemnification. SPROC will be given 5 days in which to agree to provide such indemnity.

The record also indicates that there appear to be 20 miles of right-of-way south of Curtiss over which SPROC holds only an easement. As to this portion, SPROC shall convey whatever interest it holds in the ROW by quitclaim deed. Quitclaim deeds transfer all interest that a carrier has in the property to be conveyed. The offeror will obtain all property rights that the transferring carrier has at the time of the conveyance. See Southern Pacific (citing Chesapeake

⁵ We see no justification on the record to round up this figure, as sought by SPROC. Consequently, we will not do so.

Western Railway Company—Abandonment—Between Pleasant Valley and Staunton in Rockingham and Augusta Counties, VA, Docket No. AB-290 (Sub-No. 120) (ICC served Sept. 17, 1992)).

Track and Track Materials.

As noted above, SPROC's figure of \$5,400,000 for the NSV of the track and track materials is based on Kenneth Young's appraisal report of track assets. Mr. Young estimated the NSV for the track assets at \$5,385,208 (which he rounds to \$5,400,000). SPROC Petition, Exhibit F at 11. Mr. Young states in his verified statement that he performed a site inspection of the assets to determine the condition of the rail, ties, and switches, prepared an inventory of rail and track assets, reviewed the track structure maintenance records, and researched the current relay rail and scrap rail pricing. Mr. Young's NSV for the track and track materials is uncontested by Sonora. Therefore, we will accept Mr. Young's \$5,385,208 NSV for track materials.⁶

Net Liquidation Value.

Accordingly, relying on SPROC's figure of \$247,436 for the value of the land and its figure of \$5,385,208 for the value of the track and track materials, we set the purchase price for the line at \$5,632,644.

Terms of Sale.

SPROC has requested closing conditions that differ from our customary conditions. But SPROC has presented no justification for imposing any of these additional requirements on Sonora. Thus, we will not impose any of the special closing conditions requested by SPROC.⁷

To the extent Sonora seeks indemnification by SPROC regarding environmental conditions, we will deny the request. Such a condition is beyond our standard terms, and we will not impose on SPROC, as part of a forced sale, additional expenses and burdens other than those ordinarily encountered by a carrier under 49 U.S.C. 10904.

In addition to the compensation for this line and the indemnity of title specified herein, we will impose our typical OFA terms: (1) payment is to be made by cash or certified check; (2) closing is to occur within 90 days of the service date of this decision; (3) SPROC shall

⁶ We see no justification on the record to round up this figure, as sought by SPROC. Consequently, we will not do so.

⁷ From their Terms Sheet, it appears that both SPROC and Sonora contemplate that closing could occur 45 days after the execution of their Purchase and Sale Agreement. The parties may incorporate such a term themselves by mutual agreement.

convey all property by quitclaim deed; and (4) SPROC shall deliver all releases from any mortgage within 90 days of closing. The parties may alter any of these terms by mutual agreement.

Finally, while we appreciate BLM's and CBD's interest and concerns in this matter, we are unable to act on their request. A full environmental analysis was conducted as part of this abandonment proceeding, as detailed in our February 3, 2006 decision, and our statute and rules do not contemplate any further environmental review as part of the OFA process. If a bona fide offeror asks us to set terms and conditions to enable it to buy the line, we must do so. We have no discretion, and therefore our decision to issue a decision setting terms and conditions is a ministerial act. As such, it is not a Federal action within the meaning of NEPA.

Moreover, we have no statutory authority to refuse to consider Sonora's OFA or to forgo the OFA process in order to facilitate BLM's desire to rail bank this corridor. An OFA to continue freight rail service under 49 U.S.C. 10904 takes precedence over both interim trail use/rail banking and the public use procedures. See, e.g., Central of Georgia Railway Company—Abandonment Exemption—In Atkinson, Berrien and Coffee Counties, GA, Docket No. AB-290 (Sub-No. 170X) (STB served Apr. 10, 1996).

This action will not significantly affect either the quality of the human environment or the conservation of energy resources.

It is ordered:

1. Sonora's motion for leave to file a request to set terms and conditions is granted.
2. If SPROC agrees to indemnify Sonora for title defects, it must so notify Sonora and the Board by April 18, 2006 and provide appropriate documentation therefor at settlement.
3. If SPROC indemnifies Sonora for title defects, the purchase price for the line is set at \$5,632,644; if SPROC refuses to so indemnify Sonora, the purchase price for the line will be \$5,385,208.
4. The parties must comply with the other terms of sale discussed above.
5. To accept the terms and conditions established here, Sonora must notify the Board and SPROC in writing, on or before April 24, 2006.
6. If Sonora accepts the terms and conditions established by this decision, Sonora and SPROC will be bound by this decision.

7. If Sonora withdraws its offer or does not accept the terms and conditions with a timely written notification, we will serve a decision by May 3, 2006, vacating the prior decision that postponed the effective date of the decision authorizing abandonment.

8. This decision is effective on its service date.

By the Board, Chairman Buttrey and Vice Chairman Mulvey.

Vernon A. Williams
Secretary